# INTERNATIONAL DEBT

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# INTERNATIONAL DEBT

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# INTERNATIONAL DEBT

## ISSUE DEFINITION

Few international economic issues have generated as much concern as the international debt problem. This concern has emanated from virtually all the key international financial players. Commercial banks, international financial institutions, central banks, as well as governments in both creditor and debtor countries, all had some stake in the massive rise in international lending and borrowing that occurred during the 1970s. While the accumulation of manageable levels of debt is no cause for alarm, heavily indebted developing countries experienced unmanageable debt-servicing difficulties. Simply put, many debtors lost their credit-worthiness. For these countries, their indebtedness threatened their economic development and political stability.

The nature of the international debt issue has changed measurably since its genesis in the early 1980s. The international community's primary concern in the initial stages was to protect the international financial system from the risks posed by the severe debt difficulties of a number of middle-income developing countries. These concerns have faded, however, as financial institutions have taken steps either to reduce exposures or to set aside reserves for loan losses. As commercial creditors have increasingly improved their ability to accommodate developing country debt, the focus of the issue has shifted to addressing the need for sustained economic growth in debtor countries. In many ways, this has transformed the international debt issue into a development challenge.

## BACKGROUND AND ANALYSIS

### A. Extent and Nature of the International Debt Problem

**According to recent World Bank estimates, developing country debt reached U.S. $1.81 trillion.** Slightly more than one-half of Third World debtors are experiencing moderate or severe debt burdens. Of these, 48 have been classified as "severely indebted countries." Table 1 presents a list of major "problem" debtors.

Countries that are experiencing the most difficulty in terms of their ability to repay debt are those whose debt service payments comprise a significant proportion of their export revenues. Since a relatively large proportion of the debt of the major borrowers is on commercial terms, their debt service has been even more sharply affected by past increases in interest rates than that of other debtors.

Small low-income countries such as those in sub-Saharan Africa are particularly burdened by debt. While the total value of this debt is much smaller than, for example, that incurred by financially plagued Latin American debtors, it remains extremely large in relation to these countries' production levels and their ability to generate export revenues, which, in turn, has been adversely affected by the slump in commodity prices which occurred during the 1980s. The debt problems of these poorer countries have only recently received the same degree of attention as those of the larger debtors, since the risk to the international financial system associated with their debts has not been as great.

External debt is not a problem for all developing countries. While the differences between countries are due largely to country-specific factors, certain regional similarities exist. Whereas Latin American countries for the most part have been historically eager borrowers in international capital markets, pro-Western developing countries in Asia have by and large relied mainly on domestic savings as a source of investment funds, rather than on foreign loans.

Table 1

Major Developing-Country "Problem" Debtors

| | Total Debt Outstanding, 1993 ($ U.S. billions) | Interest as a % of Exports 1993 |
|---|---|---|
| **Brazil** | **132.7** | **9** |
| **Argentina** | **74.5** | **21** |
| **Poland** | **45.3** | **5** |
| **Nigeria** | **32.5** | **14** |
| **Vietnam** | **24.2** | **3** |
| **Moroccco** | **21.4** | **12** |
| **Peru** | **20.3** | **16** |
| **Cote d'Ivoire** | **19.1** | **17** |
| **Syrian Arab Republic** | **20.0** | **3** |
| **Sudan** | **16.6** | **2** |
| **Ecuador** | **14.1** | **12** |
| **Bulgaria** | **12.3** | **5** |
| **Zaire** | **11.3** | **3** |
| **Nicaragua** | **10.4** | **28** |
| **TOTAL** | **454.7** | |

**Source: World Bank, *World Debt Tables, 1994-95 Edition*, 1994, Volume 1.**

Savings in the East Asian region averaged 25 to 30% of total production in the period 1970-82, thus allowing a high level of investment without excessive dependence on external debt. Moreover, East Asian countries adjusted to shocks from outside in the past decade by an explicit strategy to capture an increased share of export markets in labour-intensive manufactured goods.

In general, those countries following a market-oriented export strategy have been better able to withstand debt difficulties than those pursuing a more insulated strategy and have relied less on the market to guide economic policy. In most Latin American countries, exports still comprise a small share of GNP, so that there is substantial scope for export growth.

## B. Origins of the Problem

Between the mid-1970s and early 1980s the commercial banks increased their lending to middle-income developing countries by a factor of ten. Commercial bank lending began to flourish with the onset of the commodity price boom of 1972-73. Shortly thereafter, actions taken by the OPEC cartel led to a substantial increase in the price of oil. Oil exporters, with a large supply of petrodollars, deposited the excess funds for the most part safely with banks in industrialized countries. These banks in turn lent the funds out to creditworthy oil-importing developing countries, who needed financing to meet increasing current account deficits. A leading expert on international debt issues, William Cline, has estimated that the increased oil cost to non-oil-exporting countries amounted to U.S. $260 billion over the 1973-82 period.

The rapid accumulation of debt became a major burden only after the second oil shock in 1979. A combination of the following factors was responsible for the debt problem that officially surfaced in 1982: increases in the price of oil; a significant appreciation of the real value of the U.S. dollar; a large increase in U.S. interest rates and a global recession which caused a reduction in demand for debtor country exports, principally commodities. Developing countries were seriously affected by these economic changes since so much of the outstanding debt was short-term, floating-rate debt denominated in U.S. dollars.

Apart from external shocks, one factor that has worsened the external position of developing countries, particularly in Latin America, has been the level of private-sector capital outflows. The World Bank has estimated, for instance, that Argentina, Mexico and Venezuela together lost a full 70% of all net new borrowing in the 1979-82 period through capital flight. This exodus of capital was encouraged by keeping domestic interest rates artificially low to enhance local industry, thereby discouraging domestic savings; by overvalued exchange rates, which provided an incentive for residents to purchase dollar-denominated assets; and by a less than favourable domestic investment climate. All these factors combined to reduce the confidence of the citizens of these countries in their domestic economies, prompting them to seek out more attractive investment opportunities elsewhere.

Whereas developing countries' aggregate debt-service ratio increased significantly in the early 1980s, it had not changed over the course of the 1970s. Real rates of interest during the 1973-79 period remained consistently low. At these rates, it is not surprising that many developing countries thought it sensible to accumulate debt, to be serviced by increasing commodity export revenue. Thus, when speaking in aggregate terms, it is difficult to blame either the chartered banks or the recipient governments for creating the conditions of the debt problem. While certainly there were a number of individual loans that should never have been extended, by and large the consistent record vis à vis debt service capability during the 1970s made it seem reasonable to continue the lending.

Of course, some countries did overborrow and, when combined with major fiscal and monetary policy failures which were prevalent in many cases, the debt burdens became unmanageable. At the same time, the evidence suggests that insufficient control was exercised over bank exposure to a number of countries. Much short-term lending to these countries was simply not subject to adequate creditor scrutiny.

When debtors have to service debt, they require foreign currency to do so. Such currency may be obtained from export revenues, the proceeds of inbound investments or from additional external credits. If this foreign currency is not available, the debt simply cannot be serviced under existing conditions. In the early 1980s, not only did debt-servicing costs increase, but the revenues from exports declined as commodity prices fell. In addition, governments for the most part were reluctant to contain spending. Thus the foreign currency reserves of many developing countries were soon depleted, and without additional credits from banks to service their debts, many were forced to reschedule them; Mexico was the first to do so, in August 1982.

C. The Post-1982 Period

Since August 1982, the international debt problem has for the most part been reasonably well managed on a case-by-case basis. Concrete evidence of this lies in the fact that no major debt defaults and no major bank failures have occurred.

The primary vehicle used in the management of external debt has been the debt rescheduling agreement, beginning with Mexico's in 1982. A large number of debtors have had their debts rescheduled since then. In virtually all instances, the institution to coordinate negotiations between the debtor countries and the creditor banks has been the International Monetary Fund (IMF). By providing its own financing and by securing additional bank lending in exchange for debtors' agreements to make necessary domestic policy adjustments, the IMF has generally been able to defuse potential financial crises.

In order to obtain new funds with which to service debt, many debtor countries have been forced to implement economic programs approved by the IMF. These programs generally call for increased exports and a reduction in imports to facilitate debt servicing, devaluation of overvalued currencies, wage and price restraint, and reductions in domestic subsidies, all in exchange for an emergency infusion of capital. With the assistance of stringent IMF austerity measures and an improved world economy, developing country debtors were able in the aggregate to reduce their current-account deficit from $109 billion in 1981 to $38 billion in 1984. In fact, the world's two largest debtors, Brazil and Mexico, succeeded in accumulating current-account surpluses during this period.

Up to 1985, then, there was confidence that the combination of short-term debtor adjustments and resumption of OECD economic growth would help debtors through a difficult period. And for a time trade balances did improve and modest developing-country economic growth did resume. However, economic events in 1985 served to dampen the view of many experts that the international debt problem was one of short-term liquidity.

In that year, economic growth in OECD countries fell, and that in Latin American countries stalled. Inflation rates in major debtor countries rose, and the prices of key commodity exports such as oil, wheat and sugar fell, drastically in some instances. Although interest rate levels dropped, the total interest cost associated with long-term debt actually rose as the result of increases in debt brought about by rescheduling.

While the IMF austerity programs improved external account positions, the reductions in current-account deficits until 1984 had been achieved largely through reductions in imports that restricted other sectors of the economy. In 1982 and 1983, Latin American countries for instance reduced their imports by 45%. Reduced imports of materials, machinery

and spare parts depressed productive capacity and economic activity, with little room remaining for further decreases.

Latin American governments in particular argued that, while adhering to IMF austerity programs provided them with fresh funds with which to service their debt, the austerity measures agreed upon also created certain problems. In the short run, they served to increase unemployment, reduce economic growth and threaten political and social stability in the region. Economic output in Latin America, for example, fell 9% between 1981 and 1984.

As a result of these negative influences, many debtor governments soon began to realize that their debt-servicing problems were growing more and more acute with time. Some, such as Peru in 1984 and Brazil in 1987, decided to act and withheld debt-servicing payments. Others complained publicly, calling for a decrease in real interest rates and reductions in global protectionism.

Commercial bankers, for their part, became increasingly conscious of the fact that the adjustment measures taken by debtors were not providing the desired results. Many of them were of the opinion that steps taken by the developing countries were not extensive enough to correct serious internal economic inefficiencies. Realizing that the international debt problem was not temporary, banks suddenly became quite hesitant to increase their exposure to problem debtors. By 1986, new bank lending to Latin American debtors had dropped virtually to zero. It had become clear that a new strategy was required.

In order to help ease the international debt situation, the United States government presented three specific proposals to the October 1985 joint IMF-World Bank meeting. To assist the 40 poorest countries in sub-Saharan Africa, a special $2.7 billion loan fund would be created, to be administered jointly by the two international institutions. In addition, commercial banks would be urged voluntarily to lend a total of U.S. $20 billion to "problem" debtors in exchange for a commitment from these debtors to introduce responsible economic reforms. These reforms would attempt to reduce the role of government in the economy, create an improved climate for investment capital and curb inflation. The move was seen as helping to shore up new lending to debtor countries, lending which has been sharply curtailed in recent years. It was essentially a new approach, intended not to impose further austerity measures on developing countries, but to promote economic growth. Under the plan, referred to as the Baker

Plan, the World Bank and other development banks would also increase their structural lending to developing countries by U.S. $9 billion during the 1986-88 period.

Mexico was the first beneficiary of this new approach to easing the international debt burden. Officials from that country signed a U.S. $12.2 billion financing pact with the IMF, under which Mexico agreed to implement broad market-oriented economic reforms of deregulation, privatization and liberalized trade, and tighten up fiscal and monetary policy. In exchange, a generous infusion of fresh funding was to be provided over an 18-month period by the IMF, World Bank, InterAmerican Development Bank and the commercial banks. The objective of these moves was to assist Mexico with its sudden oil-related balance of payments difficulties and to help its economy resume growth.

Apart from its effect on the Mexican government, however, it is generally agreed that the Baker Plan exerted only a marginal impact on debtors experiencing major debt-servicing difficulties. New capital was slow to materialize, and proper economic policy reforms were not implemented. As economic growth continued to flounder, particularly in Latin America, increasing calls for a major new international debt initiative were voiced.

Several major Latin American debtors, undoubtedly spurred on by unilateral Brazilian action, threatened to impose their own repayment schedules on their commercial creditors. Brazil, the world's largest debtor, announced in February 1987 that it would suspend debt servicing on its commercial bank debt until a renegotiation agreement with its lenders was reached. This action was precipitated by a sudden deterioration in the country's foreign-exchange reserve situation.

Developments in Brazil caused several large U.S. banks, starting with Citicorp in May 1987, to augment their loan-loss reserve funds. By the end of 1987, the 15 largest U.S. banks had in fact raised their provisions for problem-country loans from approximately 5% to between 20 and 35% of exposure. Canadian banks also set aside special reserves to cover situations where continued debt-servicing was hampered or where it had been decided that debt exposure should be reduced.

Because of the foregoing measures, the risks faced by the banks subsided considerably. With lenders setting aside funds to protect themselves against default, and with

their capital base in a much improved position, the financial system became better equipped to deal with the next stage of the debt issue: the Brady debt reduction initiative.

It became clear that a major shift in approach towards the debt problem was required. Even though the position of creditors had improved through the protective action taken, debtors' economic prospects had not changed materially since repayment obligations had not been altered. Only if debt relief was provided on a significant scale would debtors gain. Otherwise, the situation facing debtors would have deteriorated, since the banks were reluctant to provide much needed new capital willingly, given that their incentive for "staying in the game" had been reduced. Without new financial inflows and with continued debt-servicing, it was felt that major Latin American debtors would have experienced difficulty in registering strong economic growth.

Given that the Baker Plan had proved to be largely unsuccessful in prompting additional bank financing, and that political and social conditions in certain developing countries had become fragile, there were demands for a new strategy. In March 1989, U.S. Treasury Secretary Brady made public a proposal to encourage commercial banks to negotiate voluntary debt reduction agreements with debtor countries. Debt reduction, if carried out under the Brady initiative, would be accompanied by the debtor country's commitment to introduce economic reforms designed to enhance domestic savings, to repatriate flight capital, and to attract private investment funds.

The Brady initiative represented a radical shift from the conventional approach of debt rescheduling and the layering of new debt upon old. In essence, many decision-makers realized that the payment of much of the outstanding debt of developing countries would not be forthcoming. Commercial banks, having already provided for loan losses and in many instances drawn down outstanding balances, were in a much better position to engage in reduction agreements. The developing countries had become increasingly aware of the many benefits that a move to free market policies could bring to their economic performance.

There is no better example of this than Mexico, which was the first to benefit from the Brady Plan, and which re-energized its economy through a series of well thought out policy reforms. In July 1989, Mexico and its creditor banks signed a debt reduction agreement which essentially gave lenders three options: they could reduce loans outstanding by 35%, with

the remainder exchanged for U.S.-backed Mexican government bonds; cut the rate of interest (to 6.25%); or increase lending. With this plan in place, the Mexican government has been successful in shaving off a considerable amount of its debt total. This success has prompted other countries, such as Venezuela, Costa Rica, Chile and the Philippines to take advantage of the plan.

Action has also been taken to reduce the debt obligations of the most severely indebted developed countries, especially those in the sub-Saharan region. One of the most positive recent developments in the entire international debt issue has been the realization by creditor governments, particularly the United States, that the situation in poor African countries should be treated differently from that in Latin American countries, where there is evident potential for strong economic growth. Countries such as Canada, the United Kingdom, the Netherlands, Japan, Germany and France have unilaterally transformed aid loans to poor countries into grants. Canada, for instance, forgave a total of $672 million in Official Development Assistance (ODA) debt to sub-Saharan African countries in September 1987.

Success in this regard was also achieved at the economic summit held in Toronto in June 1988. Leaders of the major industrialized countries were able to arrive at a consensus that the debt burden for the poorest countries should be reduced. Three months later, finance ministers of the seven leading industrialized nations agreed to select from the following options: cancelling a third of ODA debt; reducing interest rates by 3.5% or by half; and extending repayments over 25 years. The annual monetary benefit to African debtors from this decision was expected to total $500 million.

## D. Towards a Resolution of the Problem

Considerable progress has been achieved in the resolution of the international debt problem. The amount of debt outstanding, according to World Bank figures, has by and large stabilized after a period of substantial growth. More significantly, the ability of developing countries to service this debt, as measured most accurately by the ratio of debt servicing to export revenues, has also shown remarkable improvement. While commercial bank lending for projects other than trade financing and private investment has all but dried up, certain developing

countries have been able to access new investment funds through the international financial institutions (International Monetary Fund, World Bank) and through a growing bond market.

The success achieved vindicates the approach adopted by the international community in dealing with the debt problem. Since the summer of 1982, the case-by-case approach to the resolution of the commercial bank debt issue has largely succeeded in averting the possibility of major default. More recently, the availability of debt reduction schemes such as that entered into by Mexico has provided developing countries with a powerful incentive to implement market-based economic reforms. Clear evidence of a new approach to economic policy is evident in many Latin American countries, which have witnessed sizeable inflows of private investment funds, a return of flight capital from abroad, and the development of an active market for debt-based bonds.

While some analysts remain convinced that more broadly-based debt forgiveness initiatives are still required, it is likely that the debt issue will continue to be managed through loan-loss provisioning and/or the selective use of debt write-downs, continued emphasis on longer-term rescheduling agreements, voluntary debt-reduction agreements and, most importantly, the adoption of efficiency-raising measures by both debtor and creditor governments. It is generally still maintained that sweeping debt burden reductions will restrict future access to capital by debtors, while at the same time lessening their resolve to adopt necessary economic adjustments.

While debt-reduction agreements are an important tool in the battle to resolve current debt problems, there is a pressing need for long-term policies that could reduce the necessity for debt renegotiation in future. High-debt countries need to continue to adopt outward-looking economic policies that contribute to their long-term competitiveness and liberalize their trade regimes. Otherwise they may be faced with lower growth rates and less efficient export production. There are really only two ways in which a country can accommodate its debt burden: borrow less and reduce imports; or increase exports. And since the imposition of austerity measures in the long run is limited, the only real solution to the debt problem for many developing countries is to actively promote export expansion.

One way of increasing exports would be for debtors to implement a real devaluation of the local currency. This action would increase the value of export prices relative to domestic costs as long as wages, and therefore prices, were prevented from increasing. A real devaluation of significant size would also help to restore confidence in the currency and reverse previous outflows of capital. Developing countries could also ensure that realistic interest rates were put in place in order to deter the damaging flight of domestic capital.

There are three other broad areas where policy reform should be applied. First, government spending needs to be scrutinized, so that large structural deficits can be reduced. In addition, the domestic price system of many countries needs to be reformed, by reviewing all subsidies, credit allocation schemes and price distortions. A third step should involve the privatization of inefficient public enterprises. Policy reforms in all of the above areas may help reduce dependence on external financing.

There is also a need for both continued economic recovery and a resumption of inflows of capital to developing countries. High economic growth rates in the industrialized nations are a necessary condition for an early elimination of the debt problem. Simulations developed by Cline have indicated that increases in growth rates contribute much more significantly to reductions in the debt burden than do comparable decreases in interest rates.

Conventional commercial bank lending has proven to be difficult to obtain, given the current debt situation. Severe restraint with respect to external financing would, however, hurt the long-term economic development prospects of debtor countries. A 1987 study of the international debt problem by the Standing Senate Committee on Foreign Affairs recommended that much of the required increased financing be provided by international agencies, thereby easing pressures on over-exposed banks. In particular, the report called for increased funding of the World Bank by creditor governments, so that the Bank could increase its structural lending to financially troubled debtors willing to adopt effective adjustment policies. The international financial institutions have responded by sizeably increasing their financial commitment to developing countries. Continued support will likely be required as creditworthiness is re-established.

The situation facing severely indebted developing countries, concentrated largely in the sub-Saharan Africa region, is decidedly less favourable. There is increasing recognition

that the prospects for repayment of debt, most of which is owed to official creditors, are bleak. A special debt reduction plan may need to be devised for these countries, in order to provide them with the capital required to return to positive real economic growth.

As a final note, several innovative swapping techniques have been developed to reduce the amount of global debt outstanding. Although other arrangements have been entered into in the secondary debt market, such as outright purchase of debt by developing countries, debt-for-product swaps, and debt-for-debt transactions, one mechanism seems particularly noteworthy: the debt-for-equity swap, or debt capitalization plan.

Under this plan, external banks typically sell debt at a discount to a transnational firm with, for example, a Mexican subsidiary. The firm then transfers the loan note to its subsidiary, which cashes it in for Mexican pesos, also at a discount. The money received is then invested in productive assets within the local economy, thereby generating employment and economic growth. In this way, the bank is able to remove an undesirable loan from its books, the Mexican government disposes of a fixed debt obligation and foreign exchange burden, and the subsidiary receives cash which can be used for investment purposes to the benefit of the host country. Alternatively, under the same plan, the banks themselves can exchange a portion of their problem debt for equity investments in the Latin American capital markets, in the process providing these countries with new financial services.

The ultimate success of debt-equity swap programs will depend on the market perception of the individual debtor countries, the structure of the specific programs, and the debtor's willingness to accept foreign investment. Certainly, countries that impose few restrictions on their debt-for-equity programs will, all things being equal, find it relatively easier to dispose of debt than countries with less liberalized regimes.

## E. Canadian Exposure

In the early 1980s, considerable concern was voiced that a debt repudiation by a major debtor such as Mexico would jeopardize the stability of the international financial system. The view at the time was that several major banks were substantially over-exposed to problem

debtors. For example, the largest U.S. banks had accumulated an exposure of almost 200% of their capital in Latin American countries.

As was mentioned above, actions taken by the international banking community have served to reduce concern about widespread bank failures. The nine major U.S. creditor banks, for example, have been able to reduce their exposure in Latin America as a percent of capital from 177% in 1982 to less than 100% currently. While the risks of major bank failures arising from major debt repudiations or defaults have not been removed, they have thus been significantly lessened.

Canadian banks, for their part, have been prudently setting aside reserves for future loan losses. For the 32 countries deemed by the Superintendent of Financial Institutions to be in financial trouble, the chartered banks have on average set aside reserves equal to approximately 70% of loan exposure. This action has lowered the banks' exposure after reserves to about $4 billion, well below the figure of several years ago.

The previous federal government provided a sizeable inducement for the banks to undertake the creation of reserves. Increases in loan-loss reserves have come about partly because of the government's decision to permit banks to deduct from their taxable income the full value of reserves the Superintendent required to be set aside for the financially troubled debtors. The cost to the taxpayer of such deductions against anticipated losses could turn out to be significant, in view of the large exposure of Canadian banks to these countries.

In January 1995, the Bank of Canada increased its existing line of credit for Mexico to $1.5 billion. This financial vehicle is available, upon request, to assist Mexico in its short-term efforts to stabilize the country's currency.

Canada is also owed a significant amount of debt previously provided on a government-to-government basis in the form of Official Development Assistance (ODA). Recent figures place total ODA debt owed to the Canadian International Development Agency (CIDA) in the order of $3 billion, of which some $700 million was lent to sub-Saharan African countries.

To ease the debt-servicing burden of this latter group of countries, the federal government has taken several initiatives. In 1986, Canada placed a 15-year moratorium on ODA debt repayments by low-income sub-Saharan African countries. Subsequently, in September

1987, the government announced its intention to write-off totally the outstanding debts of these countries. A similar decision was made with respect to the debt owed to the Canadian government by English-speaking Caribbean countries, in March 1990. The cost to Canada of forgiving these long-term, low interest loans is relatively small.

On the trade side, the developing countries are a major market for the capital and other goods produced by more technologically advanced nations. If the developing countries are required to limit their imports or cannot acquire the necessary credits to finance additional imports, markets important for developed countries may close up, thus to some extent restricting their economic growth.

Canada has already experienced the impact of the international debt problem, particularly in its relations with the countries involved in rescheduling. The North-South Institute has estimated that between 1981 and 1987 Canada had to forgo approximately $16 billion worth of potential exports to Latin American and Caribbean debtors, owing largely to the fact that these countries had to reduce imports. While not all of the decrease in export demand for Canadian products can be attributed to external debt-servicing difficulties, these did nevertheless play an important role.

## PARLIAMENTARY ACTION

In June 1986, the Special Joint Committee of the Senate and of the House of Commons on Canada's International Relations released a report which came to several conclusions and made several recommendations in the area of international debt. In particular, the Committee called for "measures designed to promote economic recovery and development in the debtor countries," the convening of a major international conference on the external debt problem, the placing of a 15-year moratorium on repayment of Export Development Corporation loans to poor countries in sub-Saharan Africa, and improved coordination between the International Monetary Fund and the World Bank.

In April 1987, the Standing Senate Committee on Foreign Affairs published a comprehensive report on the international debt problem. The middle-of-the-road study

concluded that this problem could "only be reduced to manageable proportions through comprehensive and integrated policies worked out and adopted by the principal actors involved, including the debtor countries, the international financial institutions, the commercial banks and the creditor governments."

Included in its many recommendations were the following major measures, which, according to the Committee, could be taken to help reduce the existing debt burden:

- Provision, to a large extent by the international financial institutions, of new loans to debtor countries prepared to adopt effective economic adjustment measures

- Use of *ad hoc* debt write-downs in specific crisis situations

- Initiation of direct dialogue between creditor and debtor governments on debt issues.

In June 1990, the House of Commons Standing Committee on External Affairs and International Trade issued a report on Canada's role in solving the debt problem. The highlight of the Committee's study was the inclusion of a "framework of guiding principles" for Canadian policy makers, which contained the following elements:

- the overriding goal of international debt policy should be the achievement of sustainable human development.

- a reduction of the debt service burden of existing debt should be the first priority.

- structural adjustment programs should be backed up by sufficient financial resources, and contain policy reforms of benefit to the poor.

- Canadian support for debt relief and structural adjustment should be considered on a case-by-case basis and such relief or adjustment lending rate should not be provided to countries that abuse human rights or are not committed to economic reform.

The Committee also recommended that an international conference be held on debt and sustainable global adjustment, that the government create an advisory task force on international debt and adjustment, and that additional tax relief be provided to banks which sell

their loans "in ways that reduce the burden on debtor countries." The federal government rejected most of the Committee's recommendations.

CHRONOLOGY

| | |
|---|---|
| August 1982 - | Mexico, unable to service its debts, declared a moratorium on its payment of interest on external debt. |
| September 1984 - | The Mexican government renegotiated in principle approximately \$48.5 billion of the \$67.5 billion in loans owed to 527 foreign private banks. The payment period was extended to 14 years from six, with the first payment to begin in 1986. The Venezuelan government followed suit, by agreeing to renegotiate \$20.7 billion of a total public debt of \$27.5 billion, over a 12½ year term. |
| February 1985 - | The Brazilian government agreed to a \$45.3 billion debt rescheduling package to restructure over half the country's medium- and long-term debt. |
| October 1985 - | The United States government presented three specific proposals to the annual joint IMF-World Bank meeting to help ease the international debt situation. To assist the 40 poorest nations in sub-Saharan Africa, a special \$2.7 billion loan fund would be established and administered jointly by the IMF and the World Bank. In addition, commercial banks would be urged voluntarily to lend U.S. \$20 billion to primarily Latin American countries in exchange for a commitment from these debtors to introduce economic reforms. Finally, the World Bank and other development banks would increase their structural lending to developing countries over the next three years by \$9 billion. The initiative was known as the Baker Plan. |
| May 1986 - | The Canadian government declared a 15-year moratorium on repayment of government loans to poor nations in sub-Saharan Africa. |
| June 1986 - | The Special Joint Committee of the Senate and of the House of Commons on Canada's International Relations released its report in which several recommendations designed to help lessen the international debt problem were made. |

July 1986 - The Mexican government signed a pact with the IMF which would provide up to $12.2 billion in new credits in exchange for the implementation of market-oriented economic reforms and a tightening of fiscal and monetary policy. This agreement was the first application of the Baker initiative which was proposed in October 1985.

February 1987 - The Brazilian government suspended interest payments on U.S. $68 billion of its external debt. Payments were to resume once a renegotiation agreement was reached with creditors. This action forced several major U.S. banks to reclassify their Brazilian loans as non-performing and prompted other major Latin American debtors to consider adopting similar measures.

August 1987 - The Superintendent of Financial Institutions persuaded the Canadian chartered banks to boost loan reserves to within a range of 30-40% of the banks' exposures to 34 financially-troubled debtors.

September 1987 - Canada agreed to write-off all outstanding ODA debts of low-income sub-Saharan African countries.

December 1987 - The Bank of Boston stated its intention to write off $200 million of developing country loans. This was the first time such action had been taken by a major U.S. creditor bank.

December 1987 - The federal government presented a Ways and Means motion to Parliament, dealing with its tax reform initiative. One of the measures enabled banks to deduct from taxable income the full value of future loan-loss reserves set aside for 34 financially troubled debtors.

July 1989 - Mexico signed an agreement with its creditor banks, under the Brady Plan, which would commit these lending institutions to choose from three options: debt reduction, interest rate reduction, or increased lending.

March 1990 - Canada agreed to write off a total of $182 million in outstanding ODA debt of English-speaking Caribbean countries.

June 1990 - The House of Commons Standing Committee on External Affairs and International Trade issued its report on Canada's involvement in the international debt problem.

January 1995 - The Bank of Canada increased its existing line of credit for Mexico to $1.5 billion. This financial vehicle is available, upon request, to assist Mexico in its short-term efforts to stabilize the country's currency.

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